



APPROVED 09-28-09

**AUDIT COMMITTEE
REGULAR MEETING
4:00 p.m., Friday, August 21, 2009
City Hall, Kiva Conference Room
3939 North Drinkwater Blvd.
Scottsdale, AZ 85251**

PRESENT: Robert Littlefield, Chairman
Lisa Borowsky, Councilwoman
Suzanne Klapp, Councilwoman

STAFF: John Little, City Manager
Dan Worth, Public Works & Water Resources Division
Laverne Parker-Diggs, Human Resources Division
Scott McCarty, Financial Management Division
Richard Chess, Financial Services
Jim Flanagan, Purchasing
Bill Yazel, Purchasing
David Richert, Planning, Neighborhoods & Transportation Division
Dan Symer, Planning Department
Phil Montalvo, Tax Audit
Debora Johnson, Customer Service
Sharron Walker, City Auditor
Lisa Gurtler, Assistant City Auditor
Joyce Gilbride, Assistant City Auditor
Kyla Anderson, Senior Auditor
Leo Lew, Senior Auditor

GUESTS: Dick Bowers

Call to Order/Roll Call

Chairman Littlefield called the meeting to order at 4:03 p.m. All Committee Members were present.

1. Approval of Minutes from the Regular Meeting on July 2, 2009

COUNCILWOMAN BOROWSKI MOVED THE APPROVAL OF THE JULY 2, 2009 MEETING MINUTES. COUNCILWOMAN KLAPP SECONDED THE MOTION, WHICH CARRIED BY A UNANIMOUS VOTE OF 3-0.

2. Discussion and possible action regarding the City Treasurer job description and search

Dick Bowers, former Scottsdale City Manager, addressed the Committee, saying he thinks there are some issues with taking this action, regardless of how it is done. From his 23 years' experience with the City, he believes it is inconsistent with the Charter in two areas. It is inconsistent in the area that describes the Council role in relation to administration, and in his opinion, it is inconsistent with the section of the Charter that reflects the City Manager's role.

The city manager form of government creates a dynamic relationship that is not meant to be always completely in concert, but to blend the professionalism of people who are trained to be objective in their viewpoint with the very difficult job Councilmembers have of determining the public interest. That is sacrosanct and should remain in place. The Charter differentiates between policy and administrative roles.

Mr. Bowers said that as City Manager he worked with the former City Treasurer with no problems, and in his opinion it seems an odd governance move to spend that much money to duplicate a service when the duplication does not have the authority to bring a budget before Council. Council holds all the power to approve the budget, to adopt financial policies, and to direct the budget.

Mr. Bowers said that the Code of Ethics clearly states that Council will not do anything that the Charter forbids and will stay away from administration. What is being considered is unquestionably policy stepping into administration because the City Manager's Office cannot be separated from the budget. Mr. Bowers stated that he normally does not weigh in on City issues, but this is a very big issue that he feels strongly about. This is a governance issue, which would dramatically change the fundamental structure of a historically very successful city.

Committee Member Klapp inquired whether the former Treasurer, Jim Jenkins, reported to Mr. Bowers. Mr. Bowers responded that Mr. Jenkins reported to him as the general manager of the Department of Management Services. This is not uncommon in municipal government. The key was that the budget came to Mr. Bowers and he brought it forward to Council. Staff drew up the budget to balance Council policy direction with available funding.

Chairman Littlefield noted that Council changed the job description to clarify that it is still the responsibility of the City Manager to prepare the budget estimates as called for in the Charter. Also, many times people who work for one Charter Officer have to cooperate with people who work for another Charter Officer. Unless one believes that the employees of the City Manager are incapable of working with the employees of another Charter Officer, then the theory that everyone has to report to the City Manager is a ridiculous conclusion.

In this proposal, the Financial Services Department will work for the City Treasurer and the City Manager's employees will have to work with the City Treasurer's employees. Chairman Littlefield also noted that the City Manager's employees are already working with employees in other departments, so there is no reason they cannot do this. He believes it is an appropriate reform and stressed that this has nothing to do with the current City Manager.

Mr. Bowers said while people should cooperate, a city manager needs to have the authority to assemble, direct, review, and correct all components of the budget before it is presented to Council. He predicted that it would be challenging to find a city manager who will agree with the proposed parsing. In municipal government, budget is everything, because it is a fundamental policy document. He believes that adopting this policy is a slippery slope that has predictable consequences for the efficiency and effectiveness of the government.

Councilwoman Klapp asked how Mr. Bowers felt about moving responsibility for everything in Financial Services other than the budget to the Treasurer, who would not report on those functions to the City Manager.

Mr. Bowers replied that they function as a unit and cannot be separated. This would create a dysfunctional relationship that could not produce results. When he was City Manager, it was not his job to obey Council. Dynamic tension is intentionally built into the Charter.

Councilwoman Klapp asked Mr. Bowers if he is aware of any other city that does what this job description proposes to do.

Mr. Bowers said about 52 percent of cities with a population over 2,500 have a council manager form of government, but in the council manager structure he has never seen this.

Chairman Littlefield commented that most cities do not have an independent auditor as a charter officer, but he believes that this makes Scottsdale better. Having an independent treasurer would also make Scottsdale better. Mr. Bowers agreed that the auditor should be independent, and that as City Manager he would not want the auditor reporting to him because then he would be auditing himself. However, in his opinion, making the treasurer independent is not a wise move.

Councilwoman Borowsky said she saw no difference between this proposal and having the City Attorney be a charter officer. There is an overlay of legal input and opinions that affects most of the City Manager's decisions. To her this seems similar to the interplay between Financial Services and the City Manager.

Mr. Bower said it is dramatically different because the City Attorney's department is reactive and does not create administrative direction and documentation.

Stating that there are two job descriptions before the Committee, Chairman Littlefield said he favors the description that moves Financial Services into the City Treasurer's Department.

Councilwoman Klapp pointed out that they have a legal opinion on these two job descriptions, and she will follow that opinion by voting for the second one.

Councilwoman Borowsky agreed with Chairman Littlefield that Financial Services should be moved into the City Treasurer's Department. She inquired whether the amended language will be included. Chairman Littlefield replied that they already amended the language to deal with the issue that Councilwoman Klapp raised.

Councilwoman Klapp asked Chairman Littlefield if he contends that the job description they are recommending is consistent with the City Charter. Chairman Littlefield said he believes it is.

COUNCILWOMAN BOROWSKY MADE A MOTION TO APPROVE THE VERSION OF THE CITY TREASURER'S JOB DESCRIPTION WHICH INCLUDES SUPERVISORY AUTHORITY OVER FINANCIAL, TREASURY, AND ACCOUNTING MATTERS. CHAIRMAN LITTLEFIELD SECONDED THE MOTION, WHICH CARRIED BY A VOTE OF 2-1 (SK) .

3. Discussion of Audit Report No. 0911, In-Lieu Parking Program

Ms. Kyla Anderson presented the audit findings. The in-lieu parking program is relatively small. In the last seven years there have been 16 new participants and a total of about \$960,000 collected. The program recently moved into the Planning Division. The audit found that in-lieu parking revenues were used in accordance with the City Code. The audit found, however, that program revenues were not fully realized.

Ms. Anderson outlined the five report findings: 1) Fees were not indexed to the Consumer Price Index prior to 1993, although that was required from 1986. 2) The City resolution was not followed when charging the in-lieu parking fees. These discrepancies equate to a loss of at least \$96,000 to the downtown parking program. 3) The audit found that in-lieu fees for leased parking credits were not adjusted annually in accordance with the CPI. 4) In-lieu fees for permanent credits paid by installment did not include interest for the time value of money. 5) For two years a restaurant did not make payments for its in-lieu credits. When the restaurant was sold to new owners, City staff did not follow up to ensure that a new agreement was put into place. Ms. Anderson noted that the Division agreed with the audit findings. However, Division staff feels that the in-lieu parking fees are currently set at the market rate. Ms. Anderson noted that David Richert and Dan Symer from the Planning Division were in attendance. City Auditor Sharron Walker expressed her appreciation to the staff of the Planning Division for their assistance during the audit.

4. Discussion of Audit Report No. 0912, Use of Purchase Orders

Mr. Leo Lew reported the audit found that overall policies and procedures are in place to ensure that purchases are procured appropriately and that goods and services are received. However, the audit found two areas for improvement. First, the audit found a lack of city-wide guidance applied for the approval process for purchase requisitions. Administrative Regulation (AR) 285 regarding signature level authority states that it applies to the processing of expenditure-related documents. However, management has asserted that this does not apply to purchase requisitions and purchase orders. Secondly, ARs were not consistently followed and need to be clarified regarding methods for purchases under \$2,000. Management has agreed to revise the ARs to address both of these findings. Mr. Lew noted that representatives from Purchasing and Financial Services were in attendance.

5. Discussion of Audit Report No. 0908, Change Orders and Contract Modifications for Capital Projects

Ms. Joyce Gilbride stated that the objective of this audit was to evaluate compliance with statutory provisions, the City Procurement Code, and AR 216, which is specific to change orders and contract modifications. To complete this audit, auditors reviewed three construction projects, which included two road projects and one library, with combined budgets of \$68 million. The audit found that Capital Project Management has established multiple levels of review and approval for processing change orders, and has also developed management reports and a database for monitoring project activity. However, the audit found that significant changes to the contracts reviewed were made administratively using change orders rather than Council-approved contract modifications. AR 216 states that significant changes in price, cost, or total time to complete a project requires a contract modification. The report cites several change orders that were from 50 percent to 90 percent more than the original contract cost and more than 60 percent of the original time to complete the contract. Ms. Gilbride said that management has stated these changes were routine as they did not alter the outcome of the project. Therefore, an administrative change order was used rather than a contract modification, which would have required Council approval.

Other areas noted for improvement include: adding more information to internal reports, ensuring that policies and other authoritative documents do not contain conflicting information and are consistently followed, maintaining original documents in the contract administrator's files, and developing policies and procedures for alternative delivery contracts such as job order costing and Construction Manager at Risk. Ms. Gilbride noted that representatives from the Division were in attendance.

Chairman Littlefield noted that the management response was in disagreement with the first finding. Mr. Dan Worth said their experience with the audit team was very positive. He noted that the subject matter was very complex and the two members of the audit staff who performed most of the audit put in a lot of effort to understand their processes and systems. He explained that all parties mutually agreed on the three projects to be audited. They were chosen from among the more and demanding complex projects. The Scottsdale Road project in particular had many idiosyncratic difficulties.

Chairman Littlefield asked whether these projects were not really representative. Mr. Worth replied that in many ways they are representative, but the Scottsdale Road project in particular had multiple jurisdictions involved. The strategy was changed because they could not come to an agreement on right of way with the State Land Department. He described some of the challenges they faced with the project. These difficulties meant staff had to change the sequencing and procurement strategy, and those were addressed through modifications and change orders. He stressed that this was a very exceptional set of circumstances.

Chairman Littlefield opined that the crux of the finding is not the number of changes required but the way staff handled them. The question is whether the changes should have been approved by City Council.

Mr. Worth said there is a difference of opinion on how to interpret AR 216. The regulation uses the subjective term, defining a contract modification as a significant change to the conditions or terms of the contract.

Chairman Littlefield asked if there something that could be done to make this regulation clear. Ms. Walker told the Committee that the auditor's recommendation was to clarify when a contract modification would be used versus a change order, and the Division might want to seek Council's input on this question. The reported examples cited of increases from 50 to 90 percent, which are clearly major cost increases. The Council may want to provide some direction in terms of what should come before them for review and approval.

Chairman Littlefield noted that the management action plan states the revision is due by February 28, 2010, and the Procurement Code update is to be completed by no later than the planned annual update in June 2010.

Mr. Worth said they agree that the resolution is to make some modifications, particularly to the definitions in AR 216. However, the audit report recommends establishing a threshold. He thinks it is more complex than that. Rather than just relying on a threshold, it would be better to define specific situations that do or do not require contract modification. He elaborated that one of the change orders was for a 500 percent increase in time on the Arabian Library design contract. Although that sounds huge, it was not a significant increase. After the design contract was awarded, the project was put on a three-year hiatus by the City. The consultants did not create the delay and still performed the same work once the City arrived at a decision about Arabian Library. He believes that situations like this can be addressed more specifically in the language of the AR. Council does not need to consider every routine action.

Councilwoman Klapp advised fine-tuning the policy to avoid judgment calls as much as possible. Staff training should be done in conjunction with this. Mr. Worth agreed the AR is currently too subjective.

Chairman Littlefield said the deliverable is that staff will bring a proposed change to Council in early 2010. Mr. Worth said they propose to go through their normal AR review process, which normally does not go to Council, however they could make an exception in this case.

In response to a question from Councilwoman Klapp, Mr. Worth noted that normally the City Manager approves changes to ARs; however, adjustments must also be made to the Procurement Code and Council would see those proposed changes.

6. Discussion of the Quarterly Report for the Taxpayer Problem Resolution Officer's (TPRO) Survey Report

Ms. Walker stated that the City has a taxpayer problem resolution officer. Several years ago the former City Auditor and former City Manager agreed that the City Auditor's Office would perform that function. One of the requirements is to report the results of taxpayer satisfaction surveys to the City Council through the Audit Committee. This report is a summary of the surveys from the first two quarters of calendar year 2009.

7. Discussion regarding status of current audit progress

For this report, Ms. Walker noted that the completion dates for the audits in the Not Started group should be listed as 2010, not 2009 as the document shows.

Chairman Littlefield asked whether the audits are on schedule, and Ms. Walker affirmed that they are. She will update this report at every meeting of the Audit Committee. They are on target for completing the audit plan by June 2010 and will keep a close eye on their projects.

Councilwoman Klapp asked what the audit on boards and commissions will encompass. Ms. Walker replied that the audit objective that was approved was to look at compliance with Charter, Code, and other applicable requirements.

8. Discussion of agenda items for next Audit Committee meeting

Ms. Walker said staff expect to have one audit report to present in September, also the quarterly report on audit follow-ups. She has added an agenda item for a discussion of the status of budget and staffing, and other agenda items can be added as needed. The next meeting is scheduled for Monday, September 28th at 4:00 p.m.

Public Comment

Chairman Littlefield took public comment from Mr. Dick Bowers in conjunction with agenda item 2. No additional members of the public requested to address the Committee.

Adjournment

With no further business to discuss, being duly moved and seconded, the meeting adjourned at 4:43 p.m.

Respectfully submitted, A/V
Tronics, Inc. DBA AVTranz